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### Reform of Security over Moveable Property

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## Symposium

EdinLR Vol 16 p 261

### Reform of Security over Moveable Property

In June 2011 the Scottish Law Commission published its Discussion Paper on *Moveable Transactions*.<sup>1</sup> Much of this addresses the thorny subject of reform of security over both corporeal and incorporeal moveable property. This subject has not had a happy history either north or south of the border. The introduction of the floating charge to Scotland in 1961 has proved controversial, because although its comprehensive nature is welcome to lenders, its underlying English equity principles do not fit well with a civilian system of property law.<sup>2</sup> Further, the last forty years have seen a number of unimplemented reform proposals both in Scotland and the rest of Great Britain.<sup>3</sup>

On 28 October 2011 the Edinburgh Centre for Private Law<sup>4</sup> held a symposium on the parts of the Discussion Paper relating to security. Shortened versions of the papers follow. George Gretton, a former Scottish Law Commissioner and the principal author of the Discussion Paper, outlines the proposals. Ross Anderson subjects these to a critique in which he doubts the need for a new register of security rights. Hamish Patrick then gives his opinion as a practitioner who works in this area. Finally, Hugh Beale, who was the Commissioner responsible for the Law Commission of England and Wales' recent and unimplemented proposals to reform moveable (personal property) security, provides his assessment as an expert from south of the border.

EdinLR Vol 16 pp 261-267

### The Discussion Paper in Outline

The Scottish Law Commission project is about security over moveable property, of all types. The project includes consumer transactions. Only voluntary security is

1 Scot Law Com DP No 151, 2011.

2 See e.g. *Sharp v Thomson* 1997 SC (HL) 66.

3 See chapter 10 of the Discussion Paper.

4 <http://www.law.ed.ac.uk/centreforprivatelaw/>.

covered, so that, for example, the project does not cover liens, or rights constituted by diligence. This approach is similar to that of the UCC<sup>1</sup> and the PPSAs.<sup>2</sup> The project also includes the transfer of personal rights (ie outright assignation), but not the transfer of *other* types of moveable property, whether corporeal or incorporeal. The present paper discusses only the security side of the project.

### A. INFLUENCES: THE UCC AND THE PPSAS

Article 9 of the UCC has had great influence worldwide. Statutes that follow it closely in other countries are generally called PPSAs. The UCC and the PPSAs are not the same and the PPSAs differ among themselves. But these differences are in detail only. Whilst the Commission's project has been greatly influenced by the UCC/PPSAs, there is no question of a direct copy. The Commission's approach has been one of selective borrowing only. A comparison may be made with Quebec law, where the UCC/PPSAs have had a great influence, but were not adopted wholesale. (Indeed, Quebec law had an influence on the Commission's thinking.) Some differences between the Commission's proposals and the UCC/PPSA approach will be mentioned below.

The Commission accepted the view that underlies the UCC/PPSAs, that it should be possible to use the maximum range of moveable assets as collateral with a minimum of formality. Like the UCC and PPSAs it proposes that there should be some external act, and that where this is not delivery (for corporeals) or notice (for claims) it should be registration, not least because registration, though a formality, facilitates the use of moveable property as collateral by enabling third parties to check whether the potential borrower's assets are encumbered. Some differences from the UCC/PPSA approach are noted below.

### B. SOME HIGHLIGHTS

#### (1) A new security right

The core of the Discussion Paper (as far as security is concerned) is that Scots law should introduce a new type of moveable security right, available for both corporeal and incorporeal moveable property. As to the former, delivery would not be needed. As to the latter, notice to the account debtor would not be needed. But existing forms of security would continue to be competent. So the Discussion Paper proposes additions to, but not subtractions from, the present system. The new security could (unlike the floating charge) be granted by any type of debtor, though (as in the UCC/PPSAs) there would be limits in consumer cases.

1 The Uniform Commercial Code of the USA, which covers "secured transactions" in Article 9.

2 The Personal Property Security Acts (in some jurisdictions called Personal Property Securities Acts) which have been passed in a number of important jurisdictions and which are broadly based on Article 9 of the UCC.

In some respects it would bring Scots law “into line with”<sup>3</sup> English law, for English law allows non-possessory and non-notice security. Hence it would address the problem that was central to *Farstad Supply A/S v Enviroco Ltd*,<sup>4</sup> which is that when it comes to incorporeal property, security can be achieved only by transfer of the collateral to the creditor: *fiducia cum creditore*. By contrast, in England “equitable” security is possible. In *Farstad*, company shares were used as collateral. That necessitated the transfer of the shares to the bank. The effect was that the debtor was no longer the parent company of the company whose shares were being used as collateral. And that in turn had undesirable consequences. Under the Commission’s proposals it would become possible in Scotland, as in England, to grant a security over company shares that would take effect as a security *without* transferring title. The same would be true of intellectual property rights.

## (2) Functionality by means of civilian software

Scots law is a mixed system. But for property law the operating system is almost entirely civilian. That does not limit what can be achieved in functional terms. But it does mean that reforms, to work smoothly, must cohere with the civilian operating system. That was the problem with the floating charge, introduced in 1961.<sup>5</sup> There are those who deny that the floating charge has been problematic. But problematic it has been. I am not speaking of what the floating charge aimed at in terms of *functionality*—what appears on screen, so to speak. I am speaking about technicalities—what happens in the box under the screen. The floating charge is like a software program designed for one operating system that is made to run on another. The result is messy. The Commission has sought to design the new security to run on a civilian operating system.

Thus the new security would be a subordinate right.<sup>6</sup> As such it would not operate as a title transfer. Moreover the civilian logic about multiple subordinate rights would apply, so that more than one security can be granted over the same asset, with priority determined by the familiar principle of *prior tempore potior jure*. Thus the Discussion Paper does not envisage the need to have a complete and detailed set of rules about the new security, for the common law of security would apply automatically, except in so far as excluded, and that common law is generally satisfactory. One driver behind the enactment of UCC Article 9 and of the PPSAs was that in the Anglo-American world the common law of security is seen as unsatisfactory. Of course codification may be desirable in the longer term. But it is not necessary in the short term.

3 Though this is a phrase I dislike, for it vaguely suggests that the law was previously “out of line”, the latter phrase being one of disparagement.

4 [2011] UKSC 16, [2011] 1 WLR 921. Though an English case, it involved a secured transaction carried out under Scots law.

5 Companies (Floating Charges) (Scotland) Act 1961.

6 Subordinate personal rights (parallel to subordinate real rights) are discussed in G L Gretton, “Ownership and its objects” (2007) 71 *Rabels Zeitschrift* 802. (And if one considers, as I do, that intellectual property rights are not real rights, albeit that they are absolute like real rights, and not relative like personal rights, then one may also have subordinate rights in intellectual property rights.)

### (3) Registration

The Commission took the view that the new security should be registered, and should have its own register, provisionally called the Register of Moveable Transactions.<sup>7</sup> The main reason for registration is that what affects third parties should be discoverable by third parties: the point of security lies in its third party effect. The UCC/PPSAs take a roughly similar approach. The register would in some respects be modelled on similar registers in the USA, Canada, Australia etc. It would be online and should be cheap. In New Zealand registration costs about £1.50.

If the debtor were a company, there would be the spectre of double registration under Part 25 of the Companies Act 2006. That is already the position for land, for a security over land granted by a company must be registered *both* in the Land Register *and* in the Companies Register.<sup>8</sup> The 2006 Act introduced a new feature. Section 893 says that where a security is registered in another register – such as a security over land registered in the Land Register – an order can be made whereby information about such securities is automatically sent from that register to the Companies Register, so that the information would continue (as now) to appear in both registers, but only one actual registration would be required.<sup>9</sup> The plan would be for there to be a section 893 order whereby data registered in the new register would be automatically fed into the Companies Register.

### (4) Future assets

If the new security right can, as in the UCC/PPSAs, cover after-acquired assets, it begins to look rather like a floating charge. A question asked in the Discussion Paper is whether the new security *should* be able to cover such assets. The Discussion Paper, like the UCC/PPSAs, proposes that security over after-acquired assets should not be competent in consumer cases.

### (5) Protecting buyers

The UCC/PPSAs have certain protections for those who buy from a debtor in possession, and the Commission proposes that if a non-possessory security is introduced, protection should be part of the package. Various possible approaches are possible, and the Discussion Paper canvasses views.

## C. THE FLOATING CHARGE

If the new security can cover future assets, then it could to that extent overlap with the floating charge. So should the floating charge continue to exist, or should it disappear,

<sup>7</sup> The Discussion Paper also proposes that for outright assignments registration should be an optional alternative to notification for the purpose of completing the grantee's title. The new register would have that function too.

<sup>8</sup> This is not the place to explore the irrationalities of Part 25 of the Companies Act 2006, or to regret that the law of business organisations, though devolved to Belfast, is not to Edinburgh.

<sup>9</sup> No such order has yet been made. But the possibility is being considered for standard securities, and for floating charges once the latter obtain their own register under the Bankruptcy and Diligence etc (Scotland) Act 2007.

as in Canada, Australia and New Zealand? The Discussion Paper proposes that it should not be abolished, though of course that issue could be looked at again in some future law reform project. But the Discussion Paper does ask about whether certain reforms to the floating charge might be desirable.

#### D. EXAMPLES

##### (1) Corporeal moveables

Bob, a self-employed businessman, wishes to borrow £10,000 from his brother. His brother is willing to lend, but wants security. The only collateral Bob can offer is his van. Pledge would be competent, but impracticable, because pledge is a possessory security, and Bob cannot afford to lose possession of his van. A “sale and lease-back” type of arrangement will generally fail because of s 62(4) of the Sale of Goods Act 1979. Bob could incorporate Bob the Builder Ltd, which could then grant a floating charge. But incorporation costs money, and a floating charge is an imperfect security. So the deal is problematic. Under the Commission’s proposals, a cheap non-possessory registered security would be possible.

Another example is hotel stock. The stock is constantly changing. Assuming that the new security can cover future assets, it could be used here. It would thus work rather like a floating charge but it would not be limited to corporate debtors.

##### (2) Incorporeal moveables

Bob is owed £15,000 on a building contract. He wishes to use this as collateral for a loan. Under current law this calls for an intimated assignation in security. But he does not want his customer to know. The new security would be available in such a case. It would be constituted by registration, not intimation. And suppose that he wishes to use the £15,000 as collateral for a first-ranking security to X and a second-ranking security to Y. This is almost impossible under current law, but would be easy under the proposed system. And if he wished to grant security over future contract payment rights, that too would be possible.

Suppose that Bob is the chief shareholder in Bob Ltd, and he wishes to use these shares as collateral for a loan. Under the current law that would require transfer, with the lender replacing Bob as shareholder. Under the proposed law, it could be done by registered security, title to the shares remaining in Bob.

#### E. FIXED OR FLOATING?

Would the new security be fixed or floating?<sup>10</sup> The question matters solely because of the insolvency legislation, which treats floating securities less favourably than fixed

<sup>10</sup> At the seminar on 28 October 2011 more than one speaker pointed out that the Discussion Paper imperfectly identifies the concept of “floating”. This concept was adopted into the insolvency legislation on corporate insolvency from English law, but without explanation, so that a Scots lawyer has to work it out from English law. The key point is not the “floating in” but the “floating out”. Space is lacking to discuss the issues further here. See *In re Spectrum Plus Ltd (in liquidation)* [2005] UKHL 41, [2005] 2 AC 680.

securities. One example is the “prescribed part”.<sup>11</sup> In so far as the new security is used for specific assets, such as a particular road vehicle, it would be fixed. The question becomes more difficult in so far as the new security were to be used to cover after-acquired assets as well, for then it would be behaving more like a floating charge. The Discussion Paper asks consultees for their views on this issue. Probably only one answer is possible. For the purposes of this project, the policies of the Insolvency Act 1986 have to be accepted as they are, and to the extent that the new security were to operate in a “floating” manner it would be “floating” within the meaning of the 1986 Act.

#### F. DIFFERENCES FROM THE UCC/PPSAs

It was mentioned earlier that the Discussion Paper was much influenced by the UCC/PPSAs but that there were many differences. Three may be noted here: recharacterisation, the attachment/perfection distinction, and the question of “proceeds”.

The UCC/PPSAs “recharacterise” certain title financing arrangements, such as hire purchase, leasing and conditional sale, meaning that they are regarded (roughly speaking) as full title transfers to the debtor with a security interest passing back to the creditor. Thus if X sells a truck to Y, retaining title until payment, the UCC treats the arrangement as giving X merely a security interest over the truck, with Y having full title.<sup>12</sup> The Discussion Paper asks consultees for their views, but proposes that, for the time being at least, Scots law should *not* adopt recharacterisation. This decision was partly a pragmatic one. It seemed likely that there would be strong opposition to adopting the American approach. Such opposition occurred recently in England when the English Law Commission proposed something like the US approach. Moreover, there would clearly be major difficulties in recharacterisation if it was not also being adopted in England. Finally, the Commission was concerned that recharacterisation might be forbidden by the Late Payment Directive.<sup>13</sup>

Under the UCC/PPSAs a security right effective against third parties is said to be “perfected”. But there is another possibility: “attachment”. Every perfected security is attached but not every attached security is perfected. If X grants a security over a truck to Y, but there is neither delivery nor registration, the security is attached but unperfected. An attached but unperfected security right is good as between the parties, and against certain categories of third party, but is not valid as against third parties in general. The distinction is said to be embedded in Anglo-American common law. No such distinction exists in Scots common law, and the Commission took the view that there was no reason for it to be introduced. It makes the law more

<sup>11</sup> Insolvency Act 1986 s 176A.

<sup>12</sup> This is an over-simplification, because in some respects title is indeed regarded as still being held by X. So in the USA, whether X or Y is the owner depends on what question is being asked.

<sup>13</sup> Directive 2000/35/EC.

complicated; it is simpler to have a system in which a security right either exists or does not exist. Simplicity can have costs, but the Commission thought that in this case there would be no significant costs. Thus the new security would not come into existence before registration.

In the UCC/PPSAs a security right automatically extends to the “proceeds” of collateral. So if X grants a security to Y, and X later sells the collateral in such a way that Y’s security is lost, Y takes a security over the price. There were two reasons why the SLC thought that this rule should not be adopted. The first was that (assuming that the new security right could cover after-acquired assets) it would be possible for the original security right to be drafted so as to catch the price within the security. Hence a “proceeds” rule would be of only limited practical value. The second was that a rule of this sort generates technical complexities.

### **G. REFORM ON A UK-WIDE BASIS?**

A case could be made for reform on a UK-wide basis. But in England, as here, reform has been bogged down for 40 years. Achieving reform even in one country is hard enough; two would be harder. The Commission package would be workable on a Scotland-only basis. (And it might even prompt reform in England.) Though the result of the reform would be that the law would be different on the two sides of the border, it already is different, and always has been. In one respect the reform would narrow the gap, by introducing to Scotland something functionally akin to the equitable charge.

### **H. ONE STEP AT A TIME**

Why have so many reform projects failed in the area of security over moveables? Perhaps over-ambition. The Discussion Paper has tried not to be too ambitious. It has proposed a package that would be useful, without seeking Utopia in a single leap. Probably one day further reform would be desirable. But one step at a time. And this is likely to be a sounder way of proceeding, for once the first round of reform has had the chance to bed down, what needs to be done next will be clearer than it can be at this stage.

*George L Gretton  
University of Edinburgh*

## **A Critique**

Whereas English law, in corporate and financial matters, is perceived to be the law that likes to say “yes”, Scots law sometimes appears to be the law that likes to say



“no”. The reason is often practitioner confidence. English law is arguably the most important legal system in the world. Few English practitioners ever lose much sleep over how the English courts might construe basic principles of private law, even if those principles appear stubbornly resistant to rational analysis. Scots lawyers, in contrast, tread a lonely path. They often have little modern guidance from the courts. Even where principles are tolerably clear, these may speak the language of the mercantile rather than the financial age. Scottish practitioners, who have had to work through the legal principles for themselves, thus tend to appear more cautious: for the more you know, the more you realise you do not know, and the more you worry.<sup>1</sup> The major issue of law reform in this area is to state the law in terms which are fit for modern financial practice.

There are, I think, three major issues that flow from the Scottish Law Commission’s impressive Discussion Paper on Moveable Transactions (“Discussion Paper”): (1) policy questions—what is any reform trying to achieve? (2) the lack of any fixed security for moveables; and (3) intimation of an assignation as a constitutive requirement for title transfer. Above all, however, like anyone who has tried to master the English law of security interests, I strongly support a solution that proceeds from clear principles: for “[t]here is nothing so practical as a good theory”.<sup>2</sup> This motto should be all on all practitioners’ desktops. With this in mind, I deal with these three points in turn.

### A. POLICY QUESTIONS

Scots law generally favours publicity. Publicity is one way, perhaps the paradigm way, of establishing legal certainty. It achieves a number of things. One is *data certa*. Establishing a certain date for transactions is of inestimable value for many purposes, not least insolvency (*actio Pauliana*) purposes. *Data certa* helps prevent fraud. Registration is thus a paradigm Scottish solution to achieving certainty. The Scottish Law Commission’s provisional preference for a Register of Moveable Transactions is thus quite consistent with both underlying theory and existing Scots practice.<sup>3</sup> And given the Commission’s experience with Land Registration,<sup>4</sup> we have perhaps unrivalled expertise for designing such a registration system. I would observe only that registration is not the only way.

1 A major issue for a small jurisdiction is whether comprehensive codification of Scots private law would render the law *for practitioners* more accessible than at present. If this sounds odd, imagine trying to advise on a corporate transaction without the benefit of the Companies Acts.

2 G L Gretton, “Trust and patrimony” in H L MacQueen (ed) *Scots Law into the 21<sup>st</sup> Century: Essays in Memory of W A Wilson* (1996) 182.

3 For a persuasive account of the importance of registration from a self-taught businessman rather than a lawyer (whose business endures to this day): see W Chambers, *The Assimilation of the Laws of England and Scotland, delivered at the Conversazione of the Scottish Trade Protection Society, February 3rd, 1862* (1862) 13.

4 The Land Registration etc (Scotland) Bill, at the time of writing before the Scottish Parliament and based on Scottish Law Commission’s *Report on Land Registration* (Scot Law Com No 222, 2010), will correct many of the deficiencies in the Land Registration (Scotland) Act 1979.

## B. A NEW REGISTER?

### (1) The Register of Moveable Transactions

A Register can achieve many things but not everything. Here are five difficulties with the proposed Register. First, it will not be comprehensive: “re-characterisation” of functional securities, such as retention of title clauses, has rightly been rejected. Constitution of rights in security at common law will remain possible. So any publicity, though useful, will be incomplete: a Register of Sasines for moveables, perhaps.<sup>5</sup> Secondly, moveables, whether corporeal or incorporeal, are rarely permanent. Registers of time-limited assets *are* possible – look at patents. But moveables are generally ephemeral. And a register of the ephemeral may contain more information about the dead than the living. Thirdly, the Register highlights an asymmetry: the registration of the limited right (the security) is not mirrored, as with land and registered intellectual property rights (IPRs), by registration of the primary or mother right. With land or registered IPRs, the primary right – ownership of the land, or title to the patent – is registered too; the Register, in contrast, will be a register only of limited rights.<sup>6</sup> Fourthly, it is not immediately obvious how the extent of the security rights, often in immaterial objects, will be specified. Specification obvious in one context may not be obvious in another. Pointing out to a friend your favourite exhibit, while in the *Musée du Louvre*, is one thing; pointing to the exhibit while sitting in your office in St Vincent Street is quite another. Finally, those most likely to use the register – sophisticated, professionally advised financiers – have limited need for the Register because it tells them what they already know. The information sophisticated parties really need is normally obtained during a due diligence process, by forcing the debtor to disclose copies of all security documents. Those who cannot force such disclosure, in contrast – the unsophisticated parties – are perhaps unlikely to avail themselves of the Register at all. What then is the point of a new Register? Not all legal problems, in short, can be solved by the simple expedient of requiring publicity and registration.<sup>7</sup>

### (2) Alternatives to a new register

#### (a) *The Court Books*

But suppose for now that registration is a desirable solution. Is a new register required? Scots law already has an effective register utilised by practitioners day and daily: the Books of Council and Session (“BCS”). It also has the sheriff court books.

<sup>5</sup> I do not mean this, *per se*, to be a pejorative comparison. The Register of Sasines is, in some ways, a better register of title than the Land Register that replaced it. A persuasive case for this view was made by one of the founding partners of Maclay Murray & Spens LLP: D Murray, *Land Registers and Registration of Title in Scotland* (Glasgow, 1904) (reprinted from the *Proceedings of the Incorporated Society of Law Agents in Scotland*, held at Edinburgh on 14th October 1904) at 20-21.

<sup>6</sup> There is also the additional difficulty of how a Scottish register would relate to the UK intellectual property registers.

<sup>7</sup> See R G Anderson and J Biemans, “Reform of Assignment in Security: Lessons from the Netherlands” (2012) 16 Edin LR 24: registration is available in the Netherlands, for *data certa* purposes, but the register is not public.

The court books are not limited to corporate entities. For incorporeals, *Tod's Trs v Wilson*<sup>8</sup> (holding that registration in the BCS is not equivalent to intimation) should be overturned. An objection might be that the BCS is not fully online and does not incorporate such features as priority notices. But the solution is to bring the BCS fully into the digital age, so that it can serve as a digital, as well as a paper, archive; to make the BCS searchable online; and to introduce for BCS registration similar priority notices already available elsewhere.<sup>9</sup>

(b) *Notarial Execution*

Notarial execution is the private alternative to BCS registration. I appreciate that most practitioners' experiences of continental notarial execution is such that they would be unenthusiastic about a proposal to develop our own law of notarial execution. Continental notaries, at least in corporate completions, tend to appear expensive, cumbersome and, generally, to be avoided at all costs. But Scotland has its own notarial tradition. There is no need for Scots law to mimic the French or German notary. All Scottish notaries are solicitors.<sup>10</sup> They therefore understand client needs. And although notaries should not act *qua* notary in a matter in which they have a personal financial interest,<sup>11</sup> a qualified assistant, acting *qua* notary and not *qua* employee, is sufficiently independent to notarise a document although the firm has advised one of the parties to it.<sup>12</sup> In other words, notarial execution under Scots law could be cheap, efficient and instantaneous. Notarial execution is also internationally recognised.<sup>13</sup>

### C. INCORPOREALS: INTIMATION

Intimation has at least two purposes: (1) to establish the date of transfer; and (2) to inform the debtor. The reforms will not affect purpose (2) which is, for practical reasons, often indispensable. But the reforms have an important role to play in reforming (1). In many other systems, such as Germany,<sup>14</sup> Switzerland<sup>15</sup> and England, purpose (1) is achieved by agreement. I would favour the moment of transfer being, as

8 (1869) 7 M 1100.

9 As in the Register of Inhibitions: Titles to Land Consolidation (Scotland) Act 1868 s 155(2)(a).

10 Solicitors (Scotland) Act 1980 s 58(5). It may be queried whether the government fully understood what it was doing with this provision, for the notarial function is independent of the solicitor's. Compare the Legal Services (Scotland) Act 2010, s 2(b).

11 See *Ferrie v Ferrie's Trs* (1863) 1 M 291 at 302 per Lord Ardmillan; *XY's Trs, Petrs* 1939 SLT (Sh Ct) 10; *Fraser's Exr*; *Petr* 1955 SLT (Sh Ct) 35 (*Fraser's Exrs* was decided two months before the House of Lords gave judgment in *Hynd's Exrs*, below).

12 *Hynd's Exr v Hynd's Tr* 1954 SC 112, affirmed 1955 SC (HL) 1.

13 See Anderson and Biemans (n 7) at 56.

14 § 399 BGB: "A claim can be transferred by the creditor concluding with another party a contract (Assignment). On conclusion of the assignment, the new party becomes creditor in place of the old creditor."

15 Art 164, Swiss Obligations Law: "The creditor can assign any claim to which he is entitled without the consent of the debtor, in so far as this is not inconsistent with the law, an agreement or the nature of the legal relationship."

I outlined above, either (a) the date of notarial execution or (b) the date of registration in the BCS. Any solution that seeks to offer registration as an alternative to intimation for transfer purposes, however, *increases* formalities. For whereas, under the present law, intimation alone achieves both purpose (1) and purpose (2), anyone seeking to take advantage of the registration system is likely to have to register *and* intimate.

#### D. FIXED AND FLOATING MOVEABLE SECURITIES

A major lacuna in the Scots law of rights in security over moveables is the lack of a fixed, non-possessory limited security like the English fixed charge. That lacuna ought to be filled. A fixed security in specifically identified moveables – what I prefer to call a “Specific Conventional Hypothec” (SCH) – is important, particularly for incorporeal moveables like IPRs and company shares.<sup>16</sup> The SCH will also be particularly important for the financing of corporeal moveables such as plant and machinery. The same issues of constitutive formalities, as discussed above in relation to registration as an alternative to intimation of an assignation, arise.<sup>17</sup>

Perhaps the most difficult issues are those concerning the proposed “floating lien” – this misnomer being more accurately described as a “General Conventional Hypothec” (GCH). For although this proposed security interest is, in principle, to be born as a fixed security, it looks, smells and feels like a floating security. Unlike the floating charge, however, it remains unclear how a GCH would or could be integrated into the existing UK-wide corporate insolvency regime. This is an issue of the utmost importance. One of the advantages of a (qualifying) floating charge, over and above its character as a residual, catch-all security, is that it allows the holder to appoint an administrator.<sup>18</sup> Until enforcement of the GCH and interaction with administration is clarified, therefore, it is unlikely that the floating charge will die of natural causes: instead banks will take both a floating charge and the GCH, rather in the manner of an English-style debenture. Whether or not the floating charge survives, however, there seems little point bringing into force the provisions of the Companies Act 2006 relating to the Register of Floating Charges. If there is to be a Register for Moveable Transactions, it should be, as far as possible, a one-stop shop. In the event GCH could be integrated in the UK corporate insolvency regime, however, then there would be something to be said for abolishing the floating charge.

#### E. CONCLUSIONS

The Discussion Paper is of the highest quality. I pay tribute to its contents. The main thrust of the proposals – abolition of intimation for assignations and the introduction of a SCH – are to be welcomed. Although I think that a Register of Moveable Transactions is unnecessary, I acknowledge that registration is one way of achieving

<sup>16</sup> For some of the difficulties that can arise as a result of using title transfer for shares, see *Farstad Supply A/S v Enviroco Ltd* [2011] UKSC 16, [2011] 1 WLR 921, discussed in R G Anderson, “Scottish share pledges in the Supreme Court” (2012) 16 EdinLR 99.

<sup>17</sup> See above at C.1.

<sup>18</sup> Insolvency Act 1986 Sch B1 para 14.

certainty and publicity. My own view, however, is that the date of (notarial) execution of a security document is more in line with commercial expectations. Notarial attestation can provide additional security against fraud. This modest proposal has the added advantage of providing continuity with existing legal principles.

*Ross Gilbert Anderson*  
*University of Glasgow*

EdinLR Vol 16 pp 272-278

## A View from Practice

This paper represents the initial reaction of a banking lawyer in private practice to the Scottish Law Commission's proposals regarding a new moveable security in their Discussion Paper on Moveable Transactions.<sup>1</sup> Not all aspects of the proposals can be covered and, in particular, no comments are made regarding securities granted by consumers, beyond noting that there seems to be a good case for having different rules here.

### A. UNAMBITIOUS, PRAGMATIC OR A TROJAN HORSE?

Some who favour reform of the English law of personal property security may regard the Commission's proposals as unambitious, as, for example, recharacterisation of hire purchase and debt factoring as security transactions is not envisaged. Others north and south of the border opposed to introduction of radical changes along the lines of article 9 of the US Uniform Commercial Code may regard the proposals as a Trojan horse, which may be accepted by the sceptical for the possible continuance of existing practices but which contains in its new alternative securities a mechanism through which more radical change and uncertainty will later be imposed.

It is suggested that reality lies somewhere in between and that the Commission's proposals potentially provide some pragmatic solutions to some real commercial problems. They may also provide a foundation on which further reforms may be built, if such further reforms were seen to be beneficial. The proposals should therefore be regarded more as a measured pragmatic experiment than either a Trojan horse or lacking in ambition.

Pragmatism does, indeed, seem critical to implementation of proposed reforms here. There have been many detailed proposals over the last 40 years for the reform of the law of moveable security both in Scotland and throughout the UK and all have so far failed to be implemented.<sup>2</sup> This is partly because the reforms previously proposed

<sup>1</sup> Scottish Law Commission, Discussion Paper on *Moveable Transactions* (Scot Law Com No 151, 2011).

<sup>2</sup> See chapter 10 of the Discussion Paper.

have been seen by some as too radical and, by some in England in particular, as not required in practice.<sup>3</sup>

The relationship between Scotland and England in this field also leads to a requirement for pragmatism in reform. It is generally accepted that the Scottish law of moveable security is inadequate and that it is not acceptable to be forced into using title retention and transfer mechanisms or to ensure relevant assets are subject to English or another favourable law when Scottish fixed security over moveables is impracticable (as is normally the case) and a floating charge would provide insufficient protection. In England, on the other hand, fixed security is much more straightforward to constitute in most circumstances, but very complex in its operation. The legal imperatives for reform are very different north and south of the border. In addition, the unified nature of the Scottish and English economies and the desire for unified practices of businesses operating throughout those unified economies also require to be borne in mind.

#### **B. TESTING OUT A NEW PARALLEL SYSTEM?**

The Commission's proposals are outlined in more detail in Professor Gretton's paper.<sup>4</sup> Basically, an option would be provided to constitute a "new moveable security" by registration in a new register, such registration providing a priority point and having effects otherwise largely similar to constitution of a fixed security in the traditional manner. Existing methods of constitution, for example by assignation in security of a debt with intimation to the debtor, would remain competent in parallel with the new system.

Operating old and new systems in parallel would have some transitional advantages, as fewer changes would be required to the operating systems of those continuing to use the old legal regimes. Thus, for example, asset finance companies may continue to operate their current UK-wide title-based systems, or may choose to move over to use a new Scottish security instead of the likes of sale and lease-back of Scottish equipment, in either case adding searches for competing interests in the new Scottish register to their operating systems. If using the new Scottish security proved significantly more attractive in practice the argument would then become stronger to abolish the old legal regimes and possibly also to make further changes to the new regime. This could, indeed, constitute an interesting practical experiment regarding the advantages and disadvantages of the old and new regimes.

#### **C. IMPROVING THE OLD REGIMES?**

If some defects in the old regimes are not remedied, the new regime may, of course, prevail simply through its immunity from those defects and it seems at least arguable that obvious defects in the old regimes should be remedied, which would in turn

<sup>3</sup> See e.g. R Calnan, "What is wrong with the law of security?" in J de Lacy (ed), *The Reform of UK Personal Property Security Law: Comparative Perspectives* (2009) 162.

<sup>4</sup> See G L Gretton, "The Discussion Paper in outline" (2012) 16 EdinLR 000.

provide a proper test for the new regime. It is accordingly suggested that rules be clarified for assignments, pledges and other current securities regarding (a) the competence of security over future assets, (b) the identification of assets secured, (c) security coming into effect from a future time or subject to other conditions being satisfied and (d) the timing and formalities of intimation notices in constituting security and priority.

It is also suggested that existing forms of express security taking effect technically by title transfer, such as assignment in security, take effect instead as “proper” security when expressly so taken. In addition to permitting multiple securities to be taken using the old regimes, it would permit assets over which security has been granted under the old regimes to be subject to later security under the new regime. This would also permit the grantor of security to manage assets secured more readily prior to enforcement than under the current title-based regimes.

#### **D. OPTIONAL AND ADDITIONAL “PERFECTION” MECHANISMS?**

In addition, if old and new security regimes are to run in parallel, there seems little reason not to permit security arising under a document in the (hopefully not too tightly prescribed) form to be used for the new regime to take effect using the constitution mechanisms of the old regime, such as through possession of corporeals and intimation to contract debtors, and for securities under the old forms of documents to be capable of constitution by registration in the new register.

If reforms do improve the old regimes and effectively create optional “perfection” mechanisms for moveable security, the question then arises more clearly of the extent to which the third party protection mechanisms mentioned below should apply also to the old regimes.

It is further suggested that consideration be given to additional “proxies” to registration in the new register as a means of “perfecting” new and old types of security, such as registration of the relevant security as a charge with the Registrar of Companies under the Companies Act 2006,<sup>5</sup> as this will routinely take place for UK companies anyway.

Clearly having optional systems through which to create security may also create problems, as third parties searching for existing security will have more places to search. While modern technology should be capable of facilitating cost-efficient searching of multiple registers, problems may remain regarding traditional “perfection” mechanisms, such as intimation of assignments of book debts. Currently verifying the existence of prior assignments causes some problems for debt factors. Arguments can be made that perfection systems should in fact be narrowed rather than broadened for security over certain types of assets so that, for example, debt factors could search a register and then be certain that book debts have not been secured in favour of someone else. It is suggested that a very convincing practical argument would be required to abolish immediately old systems of security “perfection” to permit only registration for this purpose.

<sup>5</sup> Companies Act 2006 Part 25.

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### **E. “ATTACHMENT”, “PERFECTION” AND REMAINING CIVILIAN**

Many register-based moveable security systems adopt a distinction between the “attachment” and “perfection” of a security interest. These distinctions are largely alien to the civilian property concepts of Scots law.<sup>6</sup> A security holder either has a real right in security or it does not – there is thus “perfection” but no “attachment”. The Commission’s rejection of this distinction is to be welcomed. In particular, fixing a single date for constitution of a new security will permit its integration with the rest of Scots property and insolvency law in a much more straightforward way than would otherwise be the case, and the simplicity of the Scottish priority system, with its single basic priority points, will be preserved. It should, therefore, be obvious how a new security should rank with competing diligence executed by another creditor.

This is not to say that third party protections against new securities would not to some extent undermine the simplicity of the Scottish priority system, just that such protections should operate in a manner that fits in with such a system, for example by discharging the security against which the third party is protected or subrogating the third party to that security.

Similarly, civilian ways can be devised to provide some of the practical advantages of “attachment”, such as in relation to “notice filing” of prospective single transactions or of a series of transactions under the likes of a master receivables security agreement that may be used by a debt factor. While “attachment” can provide an answer here in Anglo-American systems, short term retrospective constitution of real rights and doctrines of accretion, each linked to a notice filed, could provide similar results that would fit in with the theoretical structure of Scots law. The technical errors made in introducing floating charges into Scots law and the consequent practical uncertainties should not be repeated here.

### **F. PROTECTING THIRD PARTIES**

The protection of various types of third parties dealing with various types of assets subject to a new moveable security is the single most important element of reform in this field. Clearly for some types of assets and transactions searching the new register will be practical and for others it will not. Similarly, finding the asset against which one is seeking to search on a register organised with reference to a person granting security over that asset will be easier for some types of assets than for others. This in turn will depend on the data provided for registration. Those creating security will wish for cost and efficiency reasons to provide as little data as practicable when creating security and, depending on the third party protection regime, will wish to provide as much data as possible to maximise their protection, subject to cost and efficiency arguments.

Given the breadth and complexity of the issues here, it is not proposed to comment further, save to note that discoverability from the new register, or indeed through other means, is an attractive concept, if raising uncertainties for all involved. In

<sup>6</sup> See para 9.14 of the Discussion Paper.



addition, if too many third parties are too easily protected from registered securities or the grantor is otherwise too free to dispose of secured assets, the new security will have little advantage over the current floating charge and thus be unnecessary. It would also be naïve to suppose that a new security similar in effect to a floating charge would not require to be postponed to employee and other creditor claims currently preferred to floating charges.<sup>7</sup>

As indicated above, it is arguable that if current forms of moveable security are retained and improved they should also be subject to relevant third party protections—though if a general discoverability test were applicable it is suggested that the current perfection mechanisms, such as possession and intimation, should probably normally pass it.

### G. ENFORCEMENT

Recent economic difficulties have demonstrated clearly that speed and flexibility of enforcement are critical to optimising value for creditors and have, for example, exposed the serious shortcomings of the enforcement of standard securities over land,<sup>8</sup> where floating charges covering the land in question are often enforced instead. It is therefore suggested that registration of enforcement, advertising for sale, court action and similar formal procedures are not imposed, but that a mechanism similar to the English Law of Property Act receivership is provided to facilitate work-out and that a workable means of appropriation or foreclosure is provided.

### H. DIFFERENT TYPES OF ASSETS

The proposals have rightly concentrated on contract debts and ordinary corporeal moveables as the paradigm assets, while also considering the potential applicability of the proposed new security to other categories of moveables. It is clear that different issues also impact on such categories.

Registered intellectual property is constituted under UK legislation and is registered in UK registers. There is uncertainty about the law under which a given security should be created. While making a new type of Scottish security available does not much affect this, continuing uncertainties would, as the Commission concedes,<sup>9</sup> probably lead to a continued wish for registration of “Scottish” securities in the UK intellectual property registers, casting doubt on the benefit of applying the new Scottish regime here.

There is no doubt that creating security over Scottish shares and other securities is often currently highly inconvenient, if slightly less so for dematerialised or intermediated securities. If “proper” security could be created through simple registration, that would be very useful, though for old fashioned physically registered shares using the company’s share register as a “proxy” to create a new security may be

<sup>7</sup> See para 22.17 of the Discussion Paper.

<sup>8</sup> See in particular *Royal Bank of Scotland v Wilson* [2010] UKSC 50, 2011 SC (UKSC) 66.

<sup>9</sup> Para 19.14 of the Discussion Paper.

a preferable practical option, if possibly requiring changes to the Companies Act. For such shares the new register may, however, be workable as one might expect third parties dealing with such shares to search it too.

There seems little prospect that the trading systems used for dematerialised and intermediated securities could readily accommodate carrying out searches in a new Scottish register and purchasers using such systems are therefore unlikely to do so. This does not mean that such a register could not be used to create such security but that purchasers should be protected. The position regarding the Financial Collateral Arrangements (No 2) Regulations 2003<sup>10</sup> is very similar. While the Commission argues that the financial collateral regime would not be applicable to disapply registration in the new Scottish register in order to create security, the commercial imperative of using and protecting the UK market systems makes this debate irrelevant.

Further consideration requires to be given to security over other types of moveables. Fixed security is often taken over executory contracts, for example in project finance, or over interests in limited partnerships used for investment purposes and the terms of the contracts and related agreements are significant to the security and its enforcement. Given the requirement in many such situations for *ad hoc* arrangements, such as step-in or direct agreements with various contract counterparties, it seems unlikely that current practices here could change much.

There is also an argument that the new regime should be extended to the creation of fixed security over rents from land, even though such rents are not strictly moveable property and therefore outwith the remit of the Commission's project. Assignment in security of rents does, however, present very similar issues in practice to assignment of book debts, particularly for large portfolios of leased properties where there is frequent turnover of leases in the period during which a fixed security is to operate. It is suggested that the new regime be extended to rents, possibly using registration in the Land Register as a "proxy" register for this purpose as it is the obvious register for third parties to search.

## I. ENGLAND

As indicated above, there is a unified UK economy with established business practices operating throughout it. It is not, therefore, practicable to introduce radical reforms such as recharacterisation of hire purchase as security in Scotland only. If, though, such reforms were being considered in England at a later date it is suggested that the new Scottish regime proposed by the Commission would be amenable to being changed to reflect any such radical change that may be agreed on a UK basis.

Similarly, it would be a mistake to abolish floating charges in Scotland while they remain generally available and used in England, given the ability of this security to deal in a straightforward and relatively uniform manner with assets throughout the UK and in various other countries and its ubiquitous use in both general and specialised situations. This does not, of course, mean that the technical operation

10 Financial Collateral Arrangements (No 2) Regulations 2003, SI 2003/3226.

of the floating charge in Scotland cannot be made to fit better with Scottish legal concepts or even treated in a similar way to securities under the new regime operating in a similar manner.

## J. CONCLUSION

As indicated above, overall the Commission's proposals are to be welcomed, as a pragmatic opportunity to remedy some significant practical defects in the Scottish law of security. They would also appear to have a better prospect of being implemented than previous attempts at reform. Whether the proposals which ultimately emerge will be implemented and whether the old Scottish regimes will then "wither" does, of course, remain to be seen.

*Hamish Patrick*

EdinLR Vol 16 pp 278-282

## A View from England

From an English perspective, the Scottish law of moveable property has a number of striking features. One, which is not within the scope of this paper but is directly relevant to it, is that there can be no assignation without intimation to the debtor. A second is the absence of non-possessory security over corporeals except by means of a floating charge. A third is that while security-like arrangements – improper securities – can be created over incorporeals, the debtor who has complied with its obligations has only a contractual right to the return of the collateral. In an era when financial institutions are not always solvent this is a major concern. So it will be no surprise that in general I strongly support the proposals in the Scottish Law Commission's Discussion Paper.<sup>1</sup> They would also bring Scottish law closer to fulfilling the aims for a modern law of security interests set out in the UNCITRAL Legislative Guide on Secured Transactions.<sup>2</sup>

### A. SECURITY OVER CORPOREAL MOVEABLES

Admittedly, non-possessory security over goods other than "large-ticket" items like ships or aircraft may be less important than it seems. Security over goods is probably only really important for smaller companies that have not established a credit rating and I wonder how many corporeal moveables they will have that they can offer by way of security. Much equipment seems to be leased or obtained on hire purchase

<sup>1</sup> Scottish Law Commission, Discussion Paper on *Moveable Transactions* (Scot Law Com No 151, 2011).

<sup>2</sup> UNCITRAL Legislative Guide on Secured Transactions (2007) paras 49-59, available at <http://www.uncitral.org/pdf/english/texts/security-lge/Terminology-and-Recs.18-1-10.pdf>.

rather than bought, while any inventory that is not the property of the supplier under a “*Romalpa*”<sup>3</sup> clause can already be made the subject of a floating charge.

Nonetheless, it would be useful to create a non-possessory security over goods. However, it is important to be precise about the “added value” of the new form of security. The Commission proposes that the debtor may be given right to dispose of the collateral free of the security and that in any event the debtor will have to power to dispose of it to a purchaser in good faith provided the sale is in the ordinary course of business.<sup>4</sup> What is then the relationship of the new form of security to the floating charge? Here the thinking<sup>5</sup> is not easy to follow.

Part of the problem may be terminological. In the US lawyers sometimes refer to a lien as floating because it covers after-acquired property.<sup>6</sup> However, they more usually seem to use “floating lien” to refer to a security over a changing pool of assets, i.e. one that gives the debtor a licence (i.e. authority) to dispose of assets free of the charge. In other words, it is the power of disposition which makes the lien floating, just as it is the right to deal with the assets without obtaining the creditor’s consent to each disposition that is the badge of the floating charge in English law.<sup>7</sup> A security which authorises the debtor to dispose of certain assets free of the charge is no more or less than a floating charge over those assets, and I think the same is true when the debtor has the effective power to dispose of the assets. The only difference would be that, rather than being a separate charge over the assets concerned, it could be combined in a single security which would not be a floating lien as regards other assets.

This might not matter except that we can expect the Insolvency Service to insist that in relation to the assets subject only to a floating lien the normal rules for floating charges must apply. Thus the expenses of liquidation, the preferential creditors and the ring-fenced fund for unsecured creditors would all have priority.<sup>8</sup> Therefore the new floating lien would do very little for secured creditors save perhaps give them a bit more flexibility as to when the security will crystallise and as to the remedies. Significant change would only occur if the Insolvency Service were persuaded either to abandon these special priorities (which seems unlikely) or to switch to an approach like that used in the New Zealand Personal Property Security Act 1999, under which the creditors concerned have priority in respect of certain classes of assets (receivables and inventory).<sup>9</sup> That makes it unnecessary to ask whether the charge is fixed or floating, which arguably is a more difficult test to apply. However, even if one could persuade them to take this radical step, I doubt we will get away entirely from the distinction between fixed and floating security. This is because in administration the administrator has the right to dispose of the assets that are subject to a floating

3 *Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 1 WLR 676.

4 Discussion Paper paras 16.28-16.47.

5 Discussion Paper paras 13.37-13.38 and ch 22.

6 Cf Discussion Paper para 13.37.

7 See *In re Spectrum Plus Ltd (in liquidation)* [2005] UKHL 41, [2005] 2 AC 680.

8 Insolvency Act 1986 ss 40 and 175, 176 and 176ZA and Companies Act 2006 s 754.

9 See NZPPS Amendment Act 2001 s 14, amending Companies Act 1993 Sch 7 cl 9; discussed in Law Commission, Report on *Company Security Interests* (Law Com No 296, 2005) paras 3.168-3.170.

charge without obtaining permission from the court or the creditor.<sup>10</sup> It is hard to see how administration could be run on any other basis, so the question would merely change in form – instead of asking whether the charge was floating we would have to ask: did the debtor have the right or power to dispose of the assets free of the charge?

Thus the new form of security will provide the opportunity to take what English lawyers call a “fixed” charge over goods unless they are the kind the debtor usually sells, which the debtor will have power to dispose of free of the charge. Over the latter – in effect the debtor’s stock-in-trade<sup>11</sup> – and any others which the security permits the debtor to dispose of, the charge will in effect be little different to a floating charge.

More thought may also be needed about whether the proceeds of disposition should be within the reach of the security. The proposal is that the security will not cover the proceeds of disposition unless this is provided expressly.<sup>12</sup> I can understand a financier taking a floating charge over a changing pool of goods such as the debtor’s inventory of goods awaiting resale without expecting that the proceeds of sale will come within the charge – the proceeds are likely to be the subject of a separate receivables financing arrangement. Whether or not the proceeds are covered can safely be left to the definition of the collateral in the charge document. However, where a charge is over other goods, and is not expressed to be a floating charge only, I would have thought financiers would expect it to cover the proceeds of either any unauthorised disposition or one that was permitted by the charge document. If I am right, the only effect of excluding proceeds from the (default) reach of the security right will be to make it *de rigueur* to add words covering proceeds.<sup>13</sup>

## B. REGISTRATION AND PRIORITY BY DATE OF REGISTRATION

I agree that security over corporeal moveables should have to be registered. The publicity principle is an important one, even if there are now major departures from it in respect of financial collateral.<sup>14</sup> Moreover, it is precisely with smaller firms that

<sup>10</sup> Insolvency Act 1986 Sch B1 para 70.

<sup>11</sup> “In the ordinary course of business” is an ambiguous phrase. It may mean “any sale that is not evidently improper” (which seems to be the meaning in English law when referring to dispositions made under a floating charge) or it may mean “whether the sale is not only in normal circumstances but is of a kind of goods that the debtor would normally sell”, i.e. of its stock-in-trade. Under the second meaning, the debtor would not be able to dispose of capital equipment (or, conversely, the buyer of capital equipment would be expected to check to see if it is subject to security). It is the second meaning which should apply in this context.

<sup>12</sup> Discussion Paper para 16.48.

<sup>13</sup> The same issue arises in relation to claims, where the Discussion Paper (para 18.11) seems to assume that the debtor will remain free to collect and use the proceeds. This seems appropriate if the security is over a changing pool of claims, as when a Central Bank advancing funds to another bank takes security over the bank’s loan book: see H Beale, M Bridge, L Gullifer and E Lomnicka, *The Law of Security and Title-Based Finance*, 2<sup>nd</sup> edn (forthcoming) ch 3. I would expect a financier taking the new form security over a company’s receivables to want the proceeds to be paid to it or placed under its control (cf *Re Spectrum Plus*), otherwise, the financier would take a floating charge.

<sup>14</sup> It is doubtful whether all the exemptions given by the Financial Collateral Arrangements Regulations 2003, SI 2003/3226 can be justified: See L Gullifer, “What shall we do about financial collateral?” (2012) 65 CLP.

publicity becomes more important, both as a means of preventing fraudulent back-dating as well as one of informing third parties, and it is with less valuable transactions that we stand to gain most from reducing search costs. Likewise, as a general rule security over incorporeal property should require registration.

The proposal is that registration should be constitutive, a necessary step in order to create the security,<sup>15</sup> rather than, as in English law, merely a means of perfection so that the security is effective against other creditors. Priority would then depend on the date of creation – in most cases, the date of registration.<sup>16</sup> Registration would also be required for an outright assignment of a claim if the assignment is not intimated to the debtor.<sup>17</sup>

This seems a straightforward and elegant solution. I have two reservations. One is that if priority is to be governed by the order of creation, the registration requirements do not go far enough. Where the claim is a trade receivable, I would make registration a requirement for outright assignment even if there has been intimation. The major problem that we have in England is that there is no practical way in which a potential receivables financier can check whether or not the receivables have been assigned – checking with the account debtors is possible when we are speaking of a few large claims, but with trade receivables it is often impractical. The Discussion Paper proposals would reduce the burden somewhat – the financier might find something on the register and therefore not have to check with the account debtor concerned – but if there were no registration of any assignment of some debts, the financier would still have to check with each account debtor. I would have thought it better to make registration the only way of effecting an outright assignment of receivables as well as security over claims. Alternatively, a registered assignment could be given priority over one created by intimation alone. A majority of respondents to the English Law Commission's proposals saw merit in requiring registration of outright assignments of receivables at least for the purposes of priority.<sup>18</sup>

This might necessitate allowing a form of “notice-filing”, rather than registration only when the transaction takes place.<sup>19</sup> Often there will be a Master Agreement under which the business will offer bundles of receivables to the financier, but the financier is not obliged to take them. An assignment takes place only if the financier accepts them. If advance filing is not permitted, the result would be that the financier would constantly be filing – a waste of time.<sup>20</sup>

The other reservation about registration being a constitutive requirement relates to financial collateral arrangements – in effect, security over securities, bank accounts

15 Discussion Paper para 3.3.

16 Discussion Paper para 3.4.

17 Discussion Paper para 3.9.

18 Law Commission, Report on *Company Security Interests* (n 9) para 4.12.

19 Creation with retroactive effect to an earlier date of registration is said to be “self-evidently undesirable” (Discussion Paper para 13.43). It is not self-evident to me. All it does is allow a party who may take a security to secure its priority. The Discussion Paper contemplates a scheme of priority notices. There is no difference in principle.

20 Hamish Patrick has suggested to me that it might be possible to analyse the Master Agreement as constituting as the security in itself, with merely the collateral being subject to the financier's acceptance.

and (since 2011<sup>21</sup>) “credit claims” i.e. sums due to banks under loan agreements. The Financial Collateral Directive is notoriously difficult to interpret. However, it seems to prevent Member States requiring registration as a condition of the creation of a security financial collateral arrangement, defined as a security arrangement under which the collateral taker has “possession or control” of the financial collateral.<sup>22</sup> This seems to require that the collateral provider be prevented from dealing with the collateral,<sup>23</sup> save in exercise of any right to substitute collateral of equal value or to withdraw excess collateral.<sup>24</sup> Thus if the collateral provider has handed over possession of the share certificates or has placed dematerialised securities held through the CREST system into an escrow account controlled by the collateral taker, or in the case of intermediated securities an arrangement has been made with the intermediary that prevents the collateral provider from dealing with the securities, registration cannot be required.<sup>25</sup> If registration is to be a condition of the creation of security interests in general, there may have to be an exception for security financial collateral arrangements.

### C. RETENTION OF TITLE DEVICES

There is not space here to deal properly with Chapter 21 of the Discussion Paper, but I commend it. Whether retention of title devices are to be made registrable is separable from whether they are re-characterised as security devices, as they are in the US and the PPSAs.<sup>26</sup> I would go further in breaking down the questions. It would be possible to require registration as a condition of effectiveness in the buyer’s or hirer’s insolvency (i.e. to make registration a perfection requirement), or merely to provide that subsequent purchasers (whether outright or by way of security) will take free of unregistered interests – in other words, to make registration merely a priority point. That would in effect reverse the decision of the House of Lords in *Moorgate Mercantile Co Ltd v Twitchings*.<sup>27</sup>

Hugh Beale  
University of Warwick

21 See the amendments to SI 2003/3226 made by SI 2010/2993, implementing changes to Directive 2002/47/EC 6 June 2002, OJ L 168/43 made by Directive 2009/44/EC of 6 May 2009, OJ L 146/37, art 2.

22 See Directive 2002/47/EC art 3(1) (as amended). See generally Beale et al, *The Law of Security and Title-Based Finance* (n 13) ch 3.

23 See Recital 10 and *Gray v G-T-P Group Ltd, Re F2G Realisations Ltd (in liquidation)* [2010] EWHC 1772 (Ch), which held that it is not sufficient that the collateral taker has practical or administrative control. It must also have the legal right to control.

24 See Directive art 2.

25 It may be required for purposes of priority.

26 Compare C von Bar, E Clive and H Schulte-Nölke (eds), *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference* (Outline Edition) (2009) Book IX, esp art IX.-1:104, which means that most of the remedies and rules of Book IX ch 7 that apply to enforcement of security interests do not apply to retention of title devices.

27 [1977] AC 890.